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IN THE

Supreme Court of the United States

October Term, 1973

No. 73-1535

LEON TROLL, as Executor of the Estate of MORRIS NEWMAN, Deceased,
Petitioner,

v.

ABRAHAM BORUT,
Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

LEON MALMAN,
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Great Neck, N. Y. 11021

April 10, 1974.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1973

No.

LEON TROLL, as Executor of the Estate of Morris Newman, Deceased,

Petitioner,

v.

ABRAHAM BORUT,

Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

The petitioner, Leon Troll, respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit entered in this proceeding on January 28, 1974.

Opinion Below

No opinion was rendered by the Court of Appeals. The opinion of the District Court (unreported) appears in the Appendix.

Jurisdiction

The judgment of the Court of Appeals for the Second Circuit was entered on January 28, 1974. This petition for certiorari was filed within 90 days of that date. This court's jurisdiction is invoked under 28 U. S. C. §1254(1).

The jurisdiction of the District Court was invoked because of diversity of citizenship, the petitioner (defendant) being a citizen of Pennsylvania and the respondent (plaintiff) being a citizen of New York.

Questions Presented

1. Whether the equitable doctrine of unconscionability applies to the facts of this case so as to defeat a claim for the equitable relief of specific performance where the amount sought to be paid is less than 1/20th of the value of the property sought to be specifically obtained.

2. Whether this court should resolve the conflict between the decision below and the decision in *Marks v. Gates*, 154 Fed. 481 (C. A. 9, 1907), where specific performance of a written contract was denied on the basis of the equitable doctrine of unconscionability because enforcement would result in the transfer of property for about 1/13th of its value.

Statement of the Case

In July, 1952, the respondent, the petitioner's decedent and three other individuals organized and became equal shareholders in a corporation (Roaring Brook Acres, Inc.) to buy and hold title to approximately 400 acres of vacant land in Putnam County, New York. This land has always been the corporation's only asset. The five individuals also signed an agreement which states that if any of them *wished* to dispose of any of his shares he was to "offer in writing * * * to sell * * * to the remaining stockholders, and the remaining stockholders shall purchase the stock so offered." (Italics supplied.) The agreement also purports to require that the purchase price be "the actual cost of the shares of stock so of-

fered." Payment for shares so purchased was in each case to be made within 60 days after the offer to sell. In addition, the agreement states that if a shareholder died the surviving shareholders would purchase and his personal representative would sell his shares on the above terms.

During the next two years the shares of three of the shareholders were brought by the decedent and the respondent. In each case the sale was a voluntary act by a consenting person. At the time of each such purchase the value of the land owned by the appellant had not increased significantly. By December, 1954, the decedent owned 70% of the shares of the corporation, at a cost to him of $6,250. The respondent owned the remaining 30% of the shares, at a cost to him of $3,000. Both parties had agreed in writing to this 70/30 relationship. This situation remained unchanged until June 3, 1972, when the decedent died.

The petitioner qualified as executor of the decedent's will on July 7, 1972. On July 6, 1972, the respondent sent to the petitioner's attorney a copy of the above shareholders' agreement with a letter stating that it was his *"intention* • • • to exercise the option and right to purchase [the decedent's] stock in [the corporation] as outlined in the agreement." (Italics supplied.) On August 6, 1972, the respondent wrote another letter to the petitioner's attorney referring to his previous letter in which he had advised "of [his] intention & readiness to exercise the option, and buy [the decedent's] stock • • •." He asked to be advised "when the [appellant] is prepared to comply with the terms of [the] agreement."

Under the terms of the agreement payment for shares being purchased was required to be made within 60 days after the death of the decedent. This 60-day period

expired on August 2, 1972. *No payment for the shares was made or tendered before August 3, 1972.*

In 1971 the corporation offered the property for sale for $200,000. No sale was made.

On August 8, 1972, a qualified and well-recognized real estate appraiser, John H. Baldwin, of Braislin, Porter & Wheelock, Inc., completed and sent to the petitioner's attorney an appraisal of the corporation's above real property. In it he concluded that the fair market value of the above land was $200,000. The respondent has admitted that this is the fair market value of the land at the time of decedent's death by failing to controvert the petitioner's Rule 9(g) statement to that effect and by failing to submit any different appraisal.

Money required to pay the real estate taxes on the property, and other expenses, was advanced to the corporation by the respondent and the decedent. These amounts were carried on the corporation's books as loans. None of these "loans" had ever been repaid. At the time of decedent's death these "loans" totalled $28,183, $10,250 of which was from the respondent and $17,978 from the decedent.

Assuming that these advances were true loans, and deducting them from the above $200,000 fair market value of the corporation's real property, the decedent's interest in that property (through his shares in the corporation) is worth 70% of the net amount ($171,817), which is $120,272. By this action the respondent seeks to buy that interest for $6,250, which is *1/20th* of the value of that interest.

REASONS FOR GRANTING THE WRIT

1. The doctrine of unconscionability is an important equitable doctrine. Its viability is implicitly questioned by the result in this case. The Supreme Court should consider and resolve this question.

The equitable doctrine of unconscionability is a significant weapon in the law's arsenal, designed to do equity and prevent injustice. Its effectiveness in doing so is illustrated by the case of *Marks v. Gates,* 154 Fed. 481 (C. A. 9, 1907), which has been cited with approval and as authoritative in varying fact situations by numerous Circuit Courts of Appeal and highest state courts, most recently in *U. S. v. Georgia-Pacific Company,* 421 F. 2d 92, 104 (C. A. 9, 1970).

In *Marks* the plaintiff unsuccessfully sought specific performance of a contract by which, in consideration for the payment of $12,225, the defendant promised in writing to give the plaintiff one fifth of all property which the defendant should acquire in Alaska. At the time the agreement was made the defendant had never been to Alaska nor did he have any property there. Subsequently he acquired property there which was stated to be worth a total of $750,000. The dismissal by the District Court of the plaintiff's complaint for specific performance "on the ground that the contract set forth in the complaint is so unjust and inequitable as not to entitle the [plaintiff] to relief" was affirmed on appeal. The Court of Appeals said:

> "• • • where the consideration is so grossly inadequate as it is in the present case, and the contract is made without any knowledge at the time of its making on the part of either of the parties thereto of the nature of the property to be af-

> fected thereby, or of its value, no equitable principle is violated if specific performance is denied * * *" (154 Fed. 481, 483).

Neither of the courts below actually considered and passed upon the viability of this doctrine. The Circuit Court affirmed without opinion. The opinion of the District Court (set forth in the Appendix) does not reflect any such consideration either. Its comment (Appendix, p. 14) is a quotation from a New York Court of Appeals case that "more than mere disparity between option price and current value * * * must be shown." But surely a price/value ratio of 1:20 is more than a *mere* disparity. Its other comment is a textual quotation which is not supported by the cases cited for it.

However, the effectiveness of the doctrine of unconscionability to prevent injustice is impaired so long as the doubt as to its applicability which is raised by the result in this case persists. The Supreme Court should remove that doubt by considering and unequivocally upholding the doctrine.

2. Review by the Supreme Court will eliminate the conflict between *Marks v. Gates*, 154 Fed. 481 (C. A. 9, 1907), decided by the Ninth Circuit Court of Appeals, and this case, decided by the Second Circuit Court of Appeals.

This conflict has been described sufficiently above and need not be elaborated further here.

3. Elementary justice requires a review and reversal of the decision below.

Equity and fairness require a reversal of the decision below because that decision leads to a wholly unjust

result—the exchange of $120,000 for $6,250. To say that this result is justified or required by the terms of the contract between the parties begs this entire question. The true function of the law is to do substantial justice, not to enforce literally the terms of contracts which produce inequitable results. Equity will not enforce a contract made as the result of a *unilateral* mistake, even though such a result defeats the expectations of the other party. This case is really not different in any way.

Conclusion

For the above reasons, a writ of certiorari should issue to review the judgment of the Second Circuit.

April 10, 1974.

Respectfully submitted,

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APPENDIX.

Opinion by Wyatt, U. S. D. J., Dated May 21, 1973

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE.]

Appearances:

Botein, Hays, Sklar & Herzberg, Esqs., Attorneys for Plaintiff, 200 Park Avenue, New York, New York 10017
Alvin H. Schulman, Esq., Stuart I. Parker, Esq., Of Counsel.

Leon Malman, Esq., Attorney for Defendant, 6 Grace Avenue, Great Neck, New York 11021.

WYATT, District Judge,

These are two motions, one by defendant for summary judgment and the other (a cross motion made after defendant had moved) by plaintiff for summary judgment. Fed. R. Civ. P. 56.

The action is for the specific performance of an agreement dated July 12, 1952.

Under date of July 12, 1952, the five stockholders of Roaring Brook Acres, Inc. (Brook; a New York corporation) made a written agreement between themselves and with Brook ("the 1952 agreement"). The effect of the 1952 agreement was to keep all stock of Brook in the hands of some or all of the five then stockholders. The 1952 agreement provided that the following statement should appear on all "shares" (presumably on the certificates):

> "This stock is transferable only in accordance with the terms of the agreement between the corporation and divers stockholders, dated July 12, 1952, and now on file with the corporation, as well as proof of due compliance therewith".

See New York Personal Property Law §176. Apparently the statement was placed on all stock certificates.

By the end of 1954, all the stock of Brook (100 shares outstanding) was owned by plaintiff Borut and by Morris Newman, 30 shares by Borut and 70 by Newman. The "actual cost" (the 1952 agreement, para 4) to Borut of his 30 shares was $3,000; the "actual cost" to Newman of his 70 shares was $6,250.

Newman died on June 3, 1972. Apparently he had been a resident and citizen of New York.

Under date of June 13, 1972, the attorney for defendant Troll, "nominated" as executor of Newman, wrote to Borut asking for information about Brook.

Under date of July 6, 1972, Borut wrote the attorney for the estate of Newman and sent him a copy of the 1952 agreement, notifying him that Borut intended "as the sole surviving stockholder to exercise the option and right to purchase" Newman's stock in Brook.

Defendant Troll, a Pennsylvania citizen, on July 7, 1972 qualified as Newman's executor; evidently the probate proceedings were in New York.

Under date of August 6, 1972, Borut wrote to the attorney for the Newman estate asking "when the . . . estate is prepared to comply with the terms" of the 1952 agreement.

On August 21, 1972, the attorney for the Newman estate wrote Borut, expressing interest in a discussion of the "estate's position" regarding the stock purchase agreement.

Believing that the estate was declining to comply with the 1952 agreement, Borut, on November 16, 1972, commenced this action for specific performance of the 1952 agreement, that the estate sell 70 shares of Brook to Borut for Newman's "actual cost" of $6,250.

Opinion by Wyatt, U. S. D. J., Dated May 21, 1973

1.

Borut is a citizen of New York; Troll, the executor, is a citizen of Pennsylvania. Although Newman was a citizen of New York, it is normally the citizenship of the executor which controls and diversity jurisdiction seems here to exist. Wright, Federal Courts (2d ed.) 95

2.

The provisions of the 1952 agreement are specific as to the restrictions on the sale of any shares. If a living stockholder wishes to sell shares, the 1952 agreement provides as follows:

> "1. That no stockholder shall sell, assign, transfer, pledge, encumber, or in any way dispose of any or all of the shares of the stock of the corporation which may now or hereafter be held or owned by him, nor shall any of such shares be transferrable, except to the remaining stockholders, in equal shares.
>
> "2. That in the event that any stockholder shall wish to dispose of any or all of his stock in the said corporation, he shall offer in writing as hereafter set forth to sell it in equal shares to the remaining stockholders, and the remaining stockholders shall purchase the stock so offered in equal shares as hereinafter set forth.
>
> "3. That every such offer shall be in writing, and shall state that the offeror offers, severally and not jointly, to sell a part or all of his stock in the Corporation; and if a part of his stock, the number of shares offered for sale; and a copy of such offer, signed by the offeror, shall be sent by registered mail, to each of the other stockholders

who may then be a stockholder of the Corporation and a party to this agreement, and a duplicate copy of such offer, so signed and mailed, shall be similarly signed and mailed to the Corporation at its then principal place of business.

"4. That within sixty (60) days from the date of such delivery, each of the said stockholders to whom a copy of the offer has been delivered, shall pay to the offeror a sum equal to a pro rata share of the actual cost of the shares of stock so offered.

"5. That simultaneously with the receipt of each such payment, the offeror shall deliver to each such remaining stockholder a pro rata portion of all his shares of stock so offered, duly endorsed in blank, with the proper federal and state transfer stamps thereunto attached, together with his written resignation as an officer and/or director of the Corporation (if he shall be an officer or director thereof, or both), together with the like resignation of any nominee of such offeror who may then be an officer and/or director of the Corporation."

If a stockholder dies, the shares of Brook held by him at the time of death are governed by the following provision of the 1952 agreement:

"6. That upon the death of any stockholder, the remaining stockholders who may then be stockholders of the Corporation and parties to this agreement shall severally purchase the shares of stock of the Corporation owned or held by the stockholder so deceased, at the time of his death, as though an offer to sell had been made by such stockholder at the date of his death, under paragraph '2' of this agreement; and the terms, pro-

> visions and conditions of this agreement shall apply to and govern the personal representative or representatives of such deceased stockholder."

By its plain terms, the 1952 agreement requires the Newman estate to sell its 70 shares of Brook to Borut for $6,250 and requires Borut to buy them at that price.

The only asset of Brook is real estate and while its exact value is uncertain, it is without dispute that the land has greatly increased in value over the more than 20 years since its purchase by Brook. Borut contests the value suggested by Troll but it is clear that the Newman shares are worth more than $100,000 or many times their "actual cost" of $6,250.

This is a situation where specific performance ought certainly to be decreed if the applicable provision of the 1952 agreement is valid.

3.

The argument for the estate is that the 1952 agreement places an invalid restraint on the alienation of the Brook shares.

We need not consider whether the restraints as between the living shareholders were invalid or not. Since at least the end of 1954 there have been only two stockholders: plaintiff Borut and decedent Newman.

The applicable provision requires that the Newman estate sell to the survivor, plaintiff Borut, the Brook shares at their "actual cost".

For twenty years, Newman, with full knowledge of the contract provision, did nothing to question its validity. His estate for the first time raises a question.

The law of New York governs in this diversity case; as noted already, Brook is a New York corporation and Borut and Newman were residents of New York.

A well known treatise states that the courts "have enforced" agreements requiring the estate of a deceased stockholder to sell to the surviving stockholders. 2 O'Neal, Close Corporations, 41.

New York appears consistently to have enforced such agreements.

An agreement between two stockholders that upon the death of one, his or her shares of stock must be sold at book value to the survivor, was enforced in *Aron v. Gillman*, 309 N. Y. 157 (1955).

Two stockholders of a corporation agreed that on the death of either, the corporation would purchase the shares of the decedent for $25,000. Specific performance was granted. *Greater N. Y. Carpet House v. Herschmann*, 258 App. Div. 649, 17 N. Y. S. 2d 483 (1st Dept. 1940) A similar agreement was enforced in *In re Klaum's Will*, 294 N. Y. S. 2d 877 (Surrogate's Court, Nassau County, 1968).

There is no discussion in the opinions cited of the validity of the agreement. It appears to be assumed. In one opinion, it has been stated: "Agreements between stockholders for the purchase and sale of stock by the one first to die have been time and again the subject of judicial determinations and have been held to be valid . . .". *Murphy v. George Murphy, Inc.*, 166 N. Y. S. 2d 290, 292 (Sup. Ct., N. Y. Cty., 1957)

There was discussion of the validity of restrictions on corporate shares in *Allen v. Biltmore Tissue Corp.*, 2 N. Y. 2d 534, 161 N. Y. S. 2d 418 (1957). The restriction was there upheld but the restriction was in the form of an option at the original price on issuance, rather than a mandatory buy-sell provision as in the case at bar. The Court said that if the provision were one "rendering the sale of the stock impossible to anyone except the corporation at whatever price it wished to pay, we would, of course, strike it down as illegal." (161 N. Y. S. 2d

at 423) The significant words here seem to be "at whatever price it wished to pay"; in the case at bar, the price is fixed at "actual cost".

The decisions on which defendant relies are clearly distinguishable. For example, in *Rafe v. Hindin,* 29 A. D. 2d 481, 288 N. Y. S. 2d 662 (2d Dept., 1968), the stock could only be sold to the other stockholder but no price was stated and the stock could not be sold to a third party without the consent of the other stockholder.

4.

The defendant argues that the disparity between the present value of the shares and their "actual cost" makes it unconscionable to enforce the agreement.

This argument was considered and rejected in the *Allen* case (cited above). Judge (then) Fuld said (161 N. Y. S. 2d at 424): ". . . the validity of the restriction on transfer does not rest on any abstract notion of intrinsic fairness of price. To be invalid, more than mere disparity between option price and current value of the stock must be shown."

No New York decision has been found which refused to enforce a buy-sell agreement because of disparity between price and value. There is a dictum in *Palmer v. Chamberlin,* 191 F. 2d 532, 540-41 (5th Cir. 1951) which might support defendant, but I decline to accept the dictum under the circumstances of the case at bar. And, as in the *Palmer* case, Newman himself took advantage of the restrictive provisions to purchase shares of Brook in the early years.

The treatise already cited states: "The courts, however, have repeatedly refused to invalidate a transfer restriction simply because it required transfer of shares at a price below their value. In some instances, the disparity has been great, the value of the shares being ten,

twenty or even over a thousand times as great as the transfer price". 2, O'Neal, at 19

Specific performance of an agreement similar to that here (except that the corporation operated a family business) was decreed where the contract price was $1 per share and the "actual value was not less than $1060 per share". *In re Mather's Estate,* 410 Pa. 361, 189 A. 2d 586 (1963)

5.

The other points made by defendant have been considered but are not of sufficient merit for discussion.

The motion of defendant for summary judgment is denied.

The motion of plaintiff for summary judgment is granted.

Settle judgment on notice.

Dated: New York, New York
May 21, 1973

INZER B. WYATT
United States District Judge